IN THE CIRCUIT COURT FOR THE COUNTY OF CHARLOTTE.

TERRY & WATKINS, RECEIVERS OF THE CHARLOTTE BANKING AND INSURANCE COMPANY, *v.* DANIEL AND OTHERS.*

November 5, 1913.

1. **Banks and Banking—Directors—Resignation—Estoppel.**—The director of a bank who hands a written resignation to the bank official who customarily receives such resignations is not liable as a director for misconduct of the bank after such resignation, if he did not act as a director after such time, notwithstanding the fact that his name as a director continued in the bank's advertisement, if such advertisement was over his protest and if he never held himself out to the public as a director. In a suit by the bank against a former director, the former director is not estopped by the representations made to the public by the bank.

2. **Banks and Banking—Directors—Acceptance of Office.**—Acceptance of office by one who is elected director is necessary to constitute him a director.

3. **Banks and Banking—Duties of Directors—When Not Liable for Defalcation of Cashier.**—Directors of a bank are not insurers of the fidelity of their agents whom they have appointed and are not responsible for losses resulting from the wrongful acts of such agents unless the loss is a consequence of their own neglect of duty. The directors are not trustees in a technical sense, the relation being rather one of agency. Knowledge of all the affairs of a bank, or of what its books and papers would show to an expert accountant, cannot be imputed to directors for the purpose of charging them with liability. Directors of a bank are entitled to commit the banking business to their duly authorized officers and they are not guilty of such gross negligence as to render themselves liable for losses to the bank when they commit the management of the entire banking business to a cashier whose character and financial standing are good, and exercise ordinary care in supervising the affairs of a bank.

Bill in Chancery by Terry & Watkins, Receivers of the Charlotte Banking and Insurance Company *v.* E. F. Daniel, F. G. Thornton, B. P. Eggleston, W. G. Williams, John H. Ingram, B. W. Leigh and the Administrator of H. C. Grigsby, directors of the said Company, to charge them with liability for the defalcation of F. C. Thornton, the cashier.

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*For the syllabus of this case and the discussion contained in the note at the end of the case, the LAW REGISTER is indebted to the courtesy of Mr. E. Warren Wall, of the Farmville, Virginia, bar.

Decree against Thornton, bill dismissed as to other parties. Opinion states the case.

Miles M. Martin, of Richmond, and *J. Tinsley Coleman,* of Lynchburg, for plaintiffs.

Meredith & Cocke and *Henry Riley,* all of Richmond, *Robert Catlett,* of Lexington, *William Leigh,* of Danville, *Hugh Gault,* of Norfolk, *Carrington & Chermside,* of Charlotte, for defendants.

OPINION.

GEORGE J. HUNDLEY, JUDGE: This is a suit by the receivers of the Charlotte Banking and Insurance Company to hold the directors of the Company liable for the defalcation of F. C. Thornton, the cashier, and the bill alleges that E. F. Daniel, F. C. Thornton, B. P. Eggleston, W. G. Williams, James H. Price, John H. Ingram, B. W. Leigh, and H. C. Grigsby, since deceased, were directors of the bank at the time of its failure. Of these, B. P. Eggleston, John H. Ingram, B. W. Leigh and H. C. Grigsby, deny that they were directors at the time the defalcation occurred. At the hearing of the cause it was conceded by the plaintiffs that the evidence showed that Leigh never had been a director and that Ingram had resigned before the defalcation occurred. Much evidence has been taken to show that B. P. Eggleston was still a director at the time the bank failed, and some to show that Grigsby was a director up to the time of his death.

B. P. Eggleston testified that he became a director in 1884 and took an active part in the affairs of the bank during the time that he remained as a director; that he attended the directors meetings and that he remained a director until May 21th, 1897, and then resigned for the reason that he did not have time to spare from his own business to attend to the affairs of the bank; that he delivered a written resignation to Thornton, the cashier of the bank, and made a memorandum of the fact at the time in a pocket diary which he kept, and exhibited his diary for inspection of counsel at the time his deposition was taken, that he never was a director after that time and that he never took the oath of a director after 1897, as had been charged: That he saw his name published in the Charlotte Gazette Advertisement after his resignation as one of the directors, but did not take it seriously as the names of many persons long dead were kept in these advertisements, amongst others, the name of his father, J. W. Eggleston, which was kept there six years after his death. That he complained to Thornton about keeping his name in the advertisement, but Thornton said that he notified the (Gazette) people about these names, but that they paid no attention to it. His explana-

tion was that it was "plate" matter set up in advance and that the paper was printed, or the greater part of it, elsewhere.

Eggleston admitted that about ten days before the closing of the bank, Mr. W. G. Williams, a director, came to see him, stating that he was just back from the eye infirmery with his eyes in bad shape, and asked him (Eggleston), to assist Mr. Daniel, the president, in an examination of the affairs of the bank. That this service was asked of him as a neighbor and friend and not as a director, and was so understood at the time, that he consented to act in this capacity, and did so. Eggleston further testifies that he had occasion to state and did state when asked about it to various business friends, that he had resigned and was no longer a director of the bank, and a large number of reliable and reputable business men testify as witnesses in support of this statement. There is no evidence in the record to contradict the evidence of Eggleston and his witnesses. It seems to the Court to be a rational explanation of the whole affair, and it is the opinion of the court that he was not a director during the period when the defalcation by the cashier was charged to have occurred, and the bill should be dismissed as to him.

As to H. C. Grigsby, the evidence against him is shadowy and uncertain, there is something said about his having admitted in conversation that he was a director, but there is no evidence that he ever accepted the position or acted as such in any capacity whatever.

In Cook on Corporations, 6 Ed. page 624, the law is stated as follows: "An acceptance of the office by one, who is elected director is necessary to constitute him a director; some direct and positive act is necessary." It is further contended by Grigsby's administrator, that his intestate was disqualified under the laws of Virginia, from being a director of the bank, because he was for many years indebted to the bank, and his stock was pledged and assigned to the bank for its full value to cover such indebtedness. This fact was conceded to be true at the hearing, and the court is of opinion that H. C. Grigsby never was a director of the bank, and never attempted to act as such, and the bill should be dismissed as to him.

This brings us to the consideration of the question of embezzlement of the funds by F. C. Thornton, the cashier. The bill charges that there was a shortage in the assets at the time it failed of $43,815.34, and this seems to be established by the report of Charles A. Peple, the expert accountant, called in by the plaintiffs, and by his deposition filed in this cause; and the bill charges that this deficit was caused by the embezzlement of the funds of the bank by Thornton the cashier. That for at least five years before the failure, the bank had been operated solely

and entirely by Thornton. That no directors meeting had been held, that no supervision of the affairs of the bank had been made by the directors, that no report as required by the laws of Virginia and the by-laws of the bank had been made, the bill further charges that F. C. Thornton has been a notorious user of opium and other drugs, and that a large part of the losses which have fallen upon the bank had been caused by the dissipated habits of the said Thornton; that his habits and loose manner of doing business were well known to the said defendant directors, that they had full notice for a long time that the affairs of the bank were not properly conducted and failed to inquire into and correct the same. But no evidence was adduced on behalf of the plaintiffs to show that the directors or the public knew of the alleged bad habits of Thornton at any time before the failure of the bank, and the uncontroverted testimony of the defendants shows that they had no such knowledge.

This case is peculiar in many respects. I know of none like it in all my examination of the authorities. No evidence has been found as to the method by which the assets of the bank were dissipated, and no definite or particularly wrongful act or error of judgment either on the part of the cashier or any other person has been proven which would tend to account for the missing money or any part of it. It is hard to resist the conclusion that the cashier embezzled the assets of the bank for the last five years after he entered upon his duties as cashier, the bank seems to have been prosperous and no evidence of any wrong was even suspected until after the first five years. Though it seems, gradually the books of the bank began to show marked carelessness and no regular entries seem to have been made either of the receipt of moneys or of their payment out on checks. In many of the accounts of depositors, the greatest looseness in this and other respects seems to have been piacticed, and the court is forced to the conclusion from the evidence in this case, that this apparent negligence was by a shrewd device of the cashier, used to cover up his abstraction of the funds of the bank. Certain it is, that not a particle of evidence exists or has been produced to show that the funds of the bank have been loaned out on paper with insufficient security. It is proven that about 90 per cent of the bills receivable found in the bank before its doors were closed was good.

No evidence whatever is produced of any fraud on the part of any of the directors; none of them seem to have borrowed of the bank money which they could not return or to have loaned the same to their friends on insufficient security as appears in many of the reported cases of bank failures. The inference can not be escaped though, that someone has abstracted the assets of the

bank, and the proof is, that for at least five years betore the failure, the entire control of its funds were in the hands of F. C. Thornton, the cashier; that he alone received deposits and issued receipts therefor, paid checks, drew cashier's checks on his own bank, and drafts on corresponding banks without supervision or control by any one. It seems to be true that the directors of the bank were negligent in the discharge of their duties, but whether they were grossly negligent so as to make them liable for the dishonest actions of the cashier, is a question that this court is called upon to decide. The court will not attempt to quote from many cases or to discuss the evidence which is very voluminous, to any great extent, but will be content with discussing the principal authorities relied upon to support the case of the plaintiffs, and by the defendants in reply thereto. The case of Marshall *v.* The F. & M. Savings Bank, *et als.,* 85 Va. 676, is the only Va. case relied upon by the plaintiffs, and the case of Briggs *v.* Spalding, 141 U. S. 132, is the principal case relied upon by the defendants. The first case was decided Jan. 28, 1891 and the latter case two years later. The case of the Alexandria Bank, *supra,* was different in many important particulars from the case at bar, in that case the president of the bank abstracted $11,000 of the funds of the bank and after that fact was discovered by the directors, they retained him in his position as president. Several of the other directors got part of the money by borrowing upon notes with insufficient security, and were instrumental in loaning money to their friends in the same way. They were not only practically guilty of fraud themselves but were largely instrumental in assisting others to obtain money in the same manner. It is true that the Court in the Alexandria case held the other directors, against whom no proof of fraud or misconduct had been offered, liable for the misconduct of the president and the other directors whether this was just and proper may raise serious doubt in the minds of thoughtful men.

In the case of Saunders *v.* Bank of Mecklenburg, 113 Va. 656, which went up from the County of Mecklenburg, Judge Keith, who delivered the opinion of the court, and who had decided the Alexandria case in the circuit court, remarked that the authority of the Alexandria case was somewhat weakened by the fact that two of the Judges dissented while one of them, Judge Hinton, concurred only in the results. This court considers that the authority of the Alexandria case was very much weakened by the fact just stated. If Judge Hinton only concurred in the results, that must mean that he did not concur in the law as stated by the Judges, Lacy and Faunteleroy. It is worthy of remark, that in the Alexandria case, the court lays great stress upon the doctrine that directors of a bank occupy the relation of trustees to the creditors

of the bank, and this doctrine is certainly not in accordance with the doctrine as laid down by the United States Supreme Court and by the courts of many of the states found in the later decisions. The better doctrine seems to be that directors are not trustees in the broadest sense of the term but only in a limited sense, holding the same relation that an agent does to his principal. Only ordinary care is required of an agent or of bank directors, while of a trustee, in its strictest sense, extraordinary care is required. There is abundant authority that bank directors are not expected to examine carefully the books of the bank, for they are not expected to be expert bank accountants, nor are they required to employ expert accountants to examine into the affairs of the bank, it is not anticipated that they will look with suspicion upon the actions of their chosen executive officer. They are supposed to select men of known probity, experience and good character for these positions. There is abundant authority of the highest character for this statement of the law as will be shown from quotations hereafter made. Before proceeding further with the citation of authorities on this position, the court desires to say that in cases of this character we must regard the conditions; directors of a country bank could not be expected to exercise as strict supervision over its affairs as the directors of city banks. In the country the directors are almost invariably men of ordinary business qualifications, working without compensation, with the exacting cares of their own business pressing upon them, and they are usually scattered about the country with no sufficient facility for meeting and discussing the affairs of the bank. This is certainly true of the Charlotte Banking and Insurance Company.

The case of Savings Bank of Louisville *v.* Caperton, 87 Ky. 306, is a case in point and very strikingly similar to the case at bar. In that case the court says, "The directors receive no compensation for their services, the benefit to be derived by them from the profits of the bank, flowing solely from their interests as stock holders, if their liability is to be measured by that imposed upon the president or the director who receives as compensation a sum equivalent to an understanding to supervise the entire affairs of the bank by an actual inspection and examination of the accounts and books of the bank as well as other duties pertaining to such a position, then there will be no question as to the liability of the directors in this case." Again the court says, "It is plain that any director if at all conversant with bookkeeping, could have gone to the individual ledger and run over the accounts of depositors and then comparing that with the blotter, ending each day's transactions, could have discovered the fraud, or it might have been discovered by ascertaining the amount due each depositor as appeared from the book, but we know of no rule or

reason that would require such an investigation by directors, and to hold them responsible for failing to discharge such a duty, would be imposing such a responsibility that no business man would assume without a compensation commensurate with the labor required." Again the court says, "Where directors by their own action cause the loss to the bank, or the corporation they represent, no doubt as to their liability can arise. Where they destroy papers known to be valuable, or cause the cashier or other officers of the bank or corporation to do that which is forbidden by the charter and loss arises, they will be held responsible." The law as laid down in this case seems to be peculiarly applicable to the case at bar, the evidence of Peple, the expert accountant, who examined the affairs of the bank, shows that he had the greatest difficulty in arriving at any conclusion as to the state of affairs. He had to resort to outside evidence gotten from the depositors who were called upon to come forward and show their certificates, and is it possible that the directors of the bank could have been more fortunate than the expert? Even if they had been required to give the time and labor necessary to discover the true condition of the bank. In fact, could the directors have discovered the fraud and embezzlement of the cashier with the books kept in the manner in which they were proven to have been kept in this case? As had been stated, they had the utmost confidence in their cashier up to the very date of the failure of the bank. He was a business man according to all the testimony, whose reputation was first rate, he was trusted not only in the affairs of the bank, but was consulted upon business matters by the people generally; he was prominent in church affairs and not a breath of suspicion had been cast upon his integrity up to that time. Is it wonderful then that the directors trusted him implicitly, and must it not have been known to the people generally that he was so trusted? And we must conclude that the action of the directors in thus allowing him to transact all the business of the bank met with the approval of those who dealt with it. Again in the case of Warriner, Receiver *v.* Penoyer, 91 Federal Rep. 587, the court says: "Before the directors can be made responsible for losses which have occurred through the mismanagement or dishonesty of a cashier, it must appear that such losses resulted as a consequence of the omission of some duty on their part. If in all probability these would have occurred just the same, notwithstanding they had been ordinarily diligent and vigilant, there is no justice in shifting them upon the directors and no principle of law to justify it. They are responsible for their own actions and omissions but not for those of co-directors, in which they have not actively participated. It seems to this court that the principle of law is there accurately and forcibly stated and that it bears strictly upon the

case at bar. There is no proof in this case that any loss resulted from the omission of any duty by the directors of the bank.

"In all probability the money of the bank would have been abstracted by the cashier, shrewd and calculating as he was, no matter how great the diligence of the directors." In the same case the court says: "It is manifest in this case that the directors relinquished the most untrammeled control of the bank to the cashier, and that their supervision of its affairs was so superficial as to be hardly more than perfunctory," but we are not satisfied that actionable negligence is imputable to them collectively or individually. They are not to be deemed remiss because they did not resort to exceptionable methods, or because they relied upon the cashier's supervision of the books and accounts, or because they reposed confidence in him, his reports of the amount and other clerical details of the assets and liabilities. They were under no duty to observe the extraordinary vigilance short of which a bank cannot be protected from the crimes conceived by a dishonest cashier. The systematic serveillance observed in large banks, especially in city banks, is not customary in small village banks." This language can be applied with equal force to the case at bar. It is true that there is no evidence that the board of directors held meetings as required by their charter and by-laws and by the law of the state, but it is proven that some of the books of the bank were lost which contained some reports of meetings of the directors, but conceded that these meetings were not held and that everything was intrusted to the cashier, the authorities heretofore quoted and one authority which the court will proceed to quote from now, clearly hold that this alone did not make them responsible for the loss by reason or the dishonesty of the cashier. It is proper to remark here before passing on, thàt at least one of the directors, Mr. W. G. Williams, did endêavor to discharge his duty and in conjunction with the clerk, did attempt to go over and verify the accounts of the cashier and the books of the bank. He was a resident of the village of Charlotte courthouse, owning a drug store very close to the bank and gave a great deal of his attention to the affairs of the bank, being frequently called upon by the cashier for that purpose. He testifies that he found nothing wrong on the occasion of his examination, and that he had the utmost confidence in and trusted the cashier to the fullest extent. None of the other directors were shown to be residents of the village except B. P. Eggleston and he was in business at Drakes Branch five miles away from the village.

The last case which this court will cite is the case of Briggs, Receiver *v.* Spalding, et als., 141 U. S. 132, this is a leading authority and if it had been decided before the Alexandria case in

85 Va., it is fair to presume that the decision of the Va. Court would have been different, and it is highly probable that if a similar case to that of Marshall *v.* Alexandria Bank should ever go to our court of appeals again, the decision will be different, though as has been stated before, that case can be easily distinguished from the case at bar.

The opinion in the Briggs Case was delivered by Mr. Chief Justice Fuller. That was a case in which the management of the affairs of the bank were left to the president for many years and the court based this decision largely upon the ground that the public in dealing with the bank must have known that fact, or would be presumed to have known it, and to have acquiesced in it. In that case, Justice Fuller, quoting from the opinion of Judge Sharswood, a most distinguished Judge of the court of appeals of Pennsylvania, says, "It is by no means a well settled point what is the precise relation which directors sustain to stockholders they are undoubtedly said in many authorities to be trustees, but that as I apprehend, is only in the general sense, as we deem an agent or any other bailee intrusted with the care and management of the property of another, it is certain that they are not technical trustees, they can only be regarded as mandataries, persons who have gratuitously undertaken to perform certain duties, and who are therefore bound to apply ordinary care and diligence but no more. We are dealing now with the responsibility to stockholders, but not to outside parties, creditors and depositors, it is unnecessary to consider what the rule may be as to them. Upon a close examination of all the reported cases, it is easily reconcilable, yet I have found no judgment or decree which has held directors to account, except when they themselves have been personally guilty of some fraud on the Corporation or have known and connived at some fraud in others, or where such fraud might have been prevented had they given ordinary attention to their duties. But it is evident that gentlemen selected by the stockholders from among their body, should not be judged by the same strict standard as agent or trustee of their private estate. Were such a rule applied no gentlemen of character and responsibility would be found willing to accept such places.

"Whatever may be the case with the trustees, a director cannot be held responsible for being defrauded; to do so would be to make his position intolerable. On the one hand I think the court should do its utmost to bring fraudulent directors to account and on the other hand, should also do its best to allow honest men to act reasonably as directors." Again in the Briggs Case the court says: "Treated as a cause of action in favor of the corporation a liability of this kind should not be lightly imposed, in the ab-

sence of any evidence of any positive misfeasance, and solely upon the ground of passive negligence, and it must be made to appear that the losses for which defendants are required to respond, were the necessary and natural consequence of omission on their part, Briggs Case, 151."

This completes the quotation from authorities which the Court thinks it necessary to make. The case has been carefully gone over and no one realizes more keenly than this Court the great harm which is done to a community by a failure such as this, and the Court is forced to the conclusion that there is no sure method known in the law by which a dishonest cashier can be prevented from robbing his bank. The only remedy which promises relief is the appointment of diligent and competent bank examiners, a thing which has recently been done in Virginia and which for a long time has been the practice of the Federal Government, and yet cases are continually occurring where bank cashiers and other officials out-wit even bank examiners, and still the scheme of plunder goes on. These remedies though can only be applied by legislative authority, and if they are not efficient the Legislature can make them more so. The Courts can only do their plain duty and in doing it, beware of injustice to innocent parties. There is no evidence whatever in this case of any misfeasance or fraudulent conduct on the part of the directors of the Charlotte Banking and Insurance Company, and however strongly the Court may realize the misfortune of the depositors in that bank, it cannot afford them a remedy which would do grave injustice to people who have been guilty of no wrong. Of course, F. C. Thornton, the Cashier and one of the Directors, is liable for his defalcation, and if a decree is desired against him it will be granted. It appears that he has already made a deed of trust and filed it in this case to secure any liability on his part. A decree may be drawn in accordance with this opinion which is made a part of the record in this case but not to be copied upon the order book.

NOTE.

Although as stated by the learned President Keith in the case of Saunders *v.* The Bank of Mecklenburg, 113 Va. 656, 75 S. E. 94, there appears to be much conflict of authority as to what is the precise relation sustained by the directors of a bank toward the corporation and its stockholders on the one hand and the depositors and creditors on the other hand, the soundness of the reasoning and the results announced in the foregoing opinion would seem to be beyond question, and it is to be hoped that this case may be passed upon by the Supreme Court of Appeals, and that the doctrine set forth therein may receive its seal of affirmance, setting at rest forever, in Virginia

at least, the question as to whether bank directors are trustees or agents.

This case is peculiar in these respects, first, that none of the directors participated in any of the frauds whatever; second, that none of the directors, their relatives or friends, derived any benefit from the frauds; third, that no appreciable amount of the bank's assets were lost by discounting bad paper or lending money on insufficient security. The proof shows simply that the assets of the bank were dissipated, and the fact of the dissipation concealed by false entries and loose bookkeeping, so that even an expert accountant was unable to ascertain the condition of the bank from the books alone, stating in his deposition for the plaintiffs, that in his opinion it would have been impossible for the directors to have discovered the frauds from the books of the bank, hence the results cannot be questioned, since the cases are unanimous in holding that directors are not required to exercise more than ordinary skill in detecting the frauds of the agents of their corporations.

However, the main interest of this case lies in the fact that to a large extent it repudiates what seems to have been the doctrine laid down in the last case decided by our Supreme Court on this question, which was Marshall *v.* Farmers,' etc., Sav. Bank, 85 Va. 676, 8 S. E. 586. This case has never been cited, except in the case of Saunders *v.* The Bank of Mecklenburg, supra, in which the learned President Keith, who heard the case at nisi prius, said that its authority is somewhat diminished by the fact that two of the judges dissented and a third concurred only in the results, thus leading us to believe that perhaps,

"A judge reversed against his will,
May be of the same opinion still."

The conflict, or apparent conflict, in the decisions of our courts as to the degree of care required of a bank director may be traced to three causes, first, the conflict between the English Doctrine and the weight of authority in the United States, both in state and federal courts; second, the loose nontechnical use of the words "trust" and "trustee" by many of the text-writers, and in many of the reported cases involving the relation between directors and corporations; Third, the often reiterated statement that in determining the liability of bank directors for their negligence, every case must be judged by its own facts.

From the beginning of the development of corporation law in England, the directors have been treated *practically* as trustees, with the whole body of stockholders as cestuis que trustent, and the courts have held them to strict account for any breach of their trust relation, thus for all *practical purposes* they are regarded as trustees when called upon in equity to account for their official conduct. However, even in England, directors are not *technically trustees*, although *practically* the same strict rules obtained as to their actions.

The New York Court of Appeals, however, has recently said that directors are *practically* trustees in their relation toward the corporation but not in their relation toward the stockholders. Bloom *v.* National United, etc., Co., 152 N. Y. 114, 46 N. E. 166.

One of the fundamental rules governing trusteeship is that the trustee cannot contract for his own profit or benefit with the subject of his trust, however reasonable and proper such a contract may be. This rule gives us a touchstone to determine whether or not any given relation is that of trustee and cestui que trust, speaking technically. In Massachusetts the Supreme Court with characteristic in-

dependence, and in recognition of actual conditions, has said in regard to a contract between a corporation and one of its directors, "It is not illegal in this country, because made with a director; very generally it has been deemed impracticable to adopt a rule which prohibits such contracts." Ft. Payne, etc., Mill *v.* Hill, 174 Mass. 224, 54 N. E. 532. In New Jersey the highest court has recently decided that a director may contract with the corporation if the contract is a fair one and if it is made without concealment, and if it is approved by a majority the stockholders in meeting assembled. Hodge *v.* United States Steel Corp., 64 N. J. Eq. 807, 53 Atl. 553. In Leavenworth County Comm'rs *v.* Chicago, etc., R. Co., 134 U. S. 688, 33 L. Ed. 1064, 10 S. Ct. 708, it was held that the action of the stockholders validated a contract in which even nine out of thirteen directors were personally interested. Such also is the rule in New York. Continental Ins. Co. *v.* New York, etc., R. Co., 187 N. Y. 225, 79 N. E. 1026.

The numerous cases in the States holding that a contract between a director and his corporation is not void, shows conclusively that, technically speaking, the relationship between the directors and their corporations is not that of trustees to cestuis que trustent.

In the case of banks particularly, much more than any other kind of corporation, the directors are continually contracting with their corporation, for a director must be a stockholder; the stockholders are usually, if not always, customers of their own bank, depositing money frequently, discounting paper, borrowing money when it is needed, and thus sustaining continuously the relation of debtor and creditor with the bank—a relation arising out of almost daily contracts.

That a director is an agent and not a trustee is further shown by the nature of the contracts made by the directors with third persons. An agent represents and acts for his principal, who may be either a natural or an artificial person. A trustee is not an agent, but is a person in whom some estate, interest or power, in or affecting property, is vested for the benefit of another. When an agent contracts in the name of his principal, the principal contracts, and is bound, but the agent is not. However, when a trustee contracts as such, unless he is bound no one is bound, for he has no principal, and as a trust estate cannot promise. The contract is therefore the personal undertaking of the trustee, and though a principal, he holds the estate only with the power and for the purpose of managing it. He is personally bound by a contract which he makes as trustee, even when designating himself as such. Taylor *v.* Davis, 110 U. S. 330, 28 L. Ed. 163, 4 S. Ct. 147.

Applying this rule to the directors of solvent corporations, it is at once seen that the directors are acting as agents, since they bind their corporation and not themselves by their contracts. As to third persons, depositors and creditors, they are certainly mere agents, since in a suit for specific performance or for breach of contract the directors are neither necessary nor proper parties.

In many of the earlier cases both in England and in the States, the expressions "trust" and "trustee" were used rather loosely and not in a technical sense with reference to corporations and their directors and officers. Thus it was said by an early text-writer on corporations that "The assets of a corporation is a trust fund for the benefit of its creditors." And "The directors of a corporation are trustees for its creditors and stockholders." These doctrines were promulgated at a time when the law of corporations was just beginning to

take form and were used with reference to cases where there were flagrant or fraudulent breaches of duty by the directors, and in which the directors were held liable, but they would have been equally liable had they been regarded as agents, so that the point to be decided was not whether the directors owed the duty of ordinary care as agents, or the duty of a higher degree of care as trustees, but whether or not they were liable for their own frauds. Thus the expressions "trust" and "trustee" were rather the dicta than the doctrine of these cases. Expressions of this kind are found in the cases of Reeves *v.* George, 49 How. Pr. 82; Koehler *v.* Black River Falls Iron Company, 2 Black 715, 17 Law Ed. 339, and in numerous other cases. In all these cases one statement is made that the directors are "trustees" for the stockholders, and that no injury which the stockholders may sustain by a *fraudulent* breach of trust may be suffered to pass without remedy. In the Cumberland Coal and Iron Company *v.* Shearman, 30 Barb. 571, it is said that the directors of a corporation are the *agents or trustees* of the stockholders. Thus it would seem that in these cases where the word "trustee" is banded about so freely, the courts were not speaking technically and did not have in mind an adjudication of the precise point as to whether the director was a trustee or an agent.

Whenever it is attempted to hold a bank director liable for his negligence, the case must be decided upon its own facts. This has led frequently to divided courts, making the confusion worse confounded, since often the dissenting judges fail to state whether they dissent from the reasoning or the results, or often fail to give opinions, and sometimes when they do they fail to use the word trustee in its technical sense or in the sense used in the opinion of the majority of the court.

In the case of Marshall *v.* The Savings Bank, supra, many of these difficulties are found. Indeed, upon a close scrutiny, it is hard to tell exactly what is the real doctrine of that case. On page 684, Morewetz on Corporations is cited: "Directors are to be regarded as mandataries and are bound to exercise only *ordinary care and prudence* and they are liable to the corporation only for what is called *crassa negligentia,* or gross negligence." The court then repudiates this doctrine by saying, "But all this is at best misleading." On page 685, the court cites the opinion of Judge Hughes, "'The *gross inattention* or *negligence* allowing *fraud* or *misconduct* on the part of the agents, officers or co-directors, which could have been prevented if they had given *ordinary care* and attention to their duties, would render the directors liable." This statement of the law is approved as the ablest exposition of the law the court has been able to find. The court continues to quote Judge Hughes, "It will abundantly appear that the managing officers of corporations are personally liable for the result of *gross negligence.*" This language is strongly similar to that of the discredited Morewetz, which the court threw into the discard on the preceding page.

The court continues to quote Judge Hughes, "If by *reckless inattention,* to the duties confided to them by their corporation, frauds and misconducts are perpetrated, which *ordinary care* on their part would have prevented, then the directors are personally liable for the losses resulting." The ghost of Morewetz accusingly appears again.

This language the court also approves in warmest terms. However, Judge Hughes' days of favor are few. He is soon selected for the discard, and toward the end of the opinion the court repudiates him along with the unfortunate Morewetz and goes back to the old

doctrine of the high degree of care which is required of a trustee, which, I think, may be said to be the doctrine of the case.

It is unquestionable that this doctrine is not in accordance with the weight of authority in the States, or the recognized better doctrine. The rule is quite clearly stated that the directors of a bank are the *agents* of the corporation, only ordinary care being required of them, and each is liable for all damages resulting from the violation of duty by him, whether from *misconduct, gross negligence* or omission. Vandycke *v.* McQuade, 57 How Pr. 65. The directors of a bank are not responsible for injury to their bank caused by their act originating in an exercise of judgment unless it is so clearly wrong as to warrant the imputation of fraud or the want of the necessary knowledge for the performance of the duty assumed by them on accepting the agency. This doctrine is followed in the case of Wallace *v.* Lincoln Sav. Bank, 89 Tenn. 630, 15 S. W. 448, in which it is said that the diligence required of directors is that ordinarily exercised by prudent men about their own affairs, which is characterized as *ordinary* diligence. If a less degree of diligence is exercised, then there is negligence, and liability attaches for loss. The cases of Briggs *v.* Spalding; Savings Bank of Louisville *v.* Caperton, and Warriner, Receiver, *v.* Penoyer, quoted at length by his honor, Judge Hundley, abundantly uphold the doctrine which he lays down in the foregoing opinion, and the authorities upholding this position might be multiplied ad infinitum. It is to be hoped that this case or a similar one may come before our Supreme Court of Appeals, and that the doctrine of the agency of directors may receive their sanction, leaving the case of Marshall *v.* The Savings Bank and its few dicta acquaintances to meditate in solitude over their lonely estate.

E. WARREN WALL.

Farmville, Va.,
Nov. 20, 1913.